

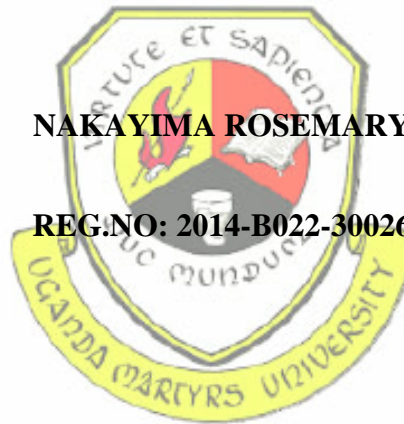
**THE CONTRIBUTION OF INTERNAL AUDITING ON THE FINANCIAL  
PERFORMANCE OF SMALL SCALE BUSINESSES**

**A CASE STUDY: BUSINESSES IN KATWE BUTEGO DIVISION MASAKA  
MUNICIPALITY**

**BY**

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**A RESEARCH REPORT SUBMITTED TO THE FACULTY OF BUSINESS  
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REQUIREMENTS FOR THE AWARD OF A BACHELOR OF BUSINESS  
ADMINISTRATION AND MANAGEMENT OF  
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## **DEDICATION**

I dedicate this dissertation to my family members who include my parents Mr. and Mrs. Matia Mutumba , my brothers Male Aloysious , Kawuma Charles and Ssekamatte Achilleo for their endeavors they have put forward to the accomplishment of this task full work.

## **ACKNOWLEDGEMENT**

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Finally I would like to have my deepest thanks to my colleagues who had played an effective role in my success and my findings in genuine thinking.

## **LIST OF ACRONYMS**

IIA	Institute of Internal Audit
SEC	Security and Exchange Commission
GAAP	General Accounting and Auditing Principles
IAS	Internal Accounting Standards
ICT	Information System and Technology

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## **ABSTRACT**

The purpose of the study was to establish how internal auditing contributes to the financial performance of small scale businesses. The study focused on the contribution of financial, information system and compliance audits in businesses of Katwe Butego Division Masaka Municipality.

The research methodology adopted both descriptive and analytical research design based on both open and closed ended questionnaires to gain an in –depth understanding of the contribution financial, information system and compliance audits. A sample of 80 respondents was used. A purposive sampling method was adopted for the study.

Data was collected from both primary data with the help of questionnaires designed using like scales and secondary data got from text books, internet, journals, articles, and news papers. Data was also obtained by use of self administered questionnaires and key informant interviews from primary source while secondary data was captured from various compendia with relevance to the study subject at hand aimed at yielding validity and reliability of data mass.

Data was analyzed using tables, percentages to establish, the contribution of the study variables. The principal benefit of this study at the end came up with the recommendations that was advance within the wider milieu of the strategic suggestions aimed at fighting poor performance of small scale businesses.

## **CHAPTER ONE**

### **GENERAL INTRODUCTION**

#### **1.0 Introduction**

The researcher focused on the contribution of internal auditing on financial performance of small scale businesses.

In this chapter, the research explored the background of the study, problem statement, the purpose and specific objectives of the study, research questions and scope of the study and subsequently the definition of the terms and concepts used, the significance of the study, justification of the study, conceptual frame work, Limitations and conclusions.

#### **1.1.0 Background to the study**

##### **1.1.1 Historical background**

The demand for both external and internal auditing is sourced in the need to have some means of independent verifications to reduce record keeping errors, asset misappropriation and fraud with in the business and non business organizations (Richard 1905).

The task of hearing the accounts gave rise to the term audit, originating from Latin audit us or audire, which means a hearing or to hear or listen. These hearings played an important role at that time since not many people could read or write. The auditors were selected by the community and were expected to be competent and professional in recognizing fraud and errors. (Dittenhofer 1984)

At the beginning of the 13<sup>th</sup> century the first two official state auditors were appointed in the city of Pisa as an internal and external auditors (Filius, 1984). This led to the practice of keeping two parallel sets of books for audit purpose.

According to Kaplan et al (1987) to oversee these diverse and dispersed operations, new procedures were invented, accompanied by effective management accountancy systems to coordinate the logistic, conversion and distribution activities.

He further suggests that in the 1840 when the railway firms began to conduct large scale financial transactions at widely dispersed geographical locations, they appointed internal auditors' to monitor the processing of financial transactions for example payment vouchers, cash balances.

As firms become larger and more complicated and therefore management's ability to monitor its operations became more limited, the role of internal audit functions increased (Sawyer 1996) in most cases, the internal audit function was a sub function of the accounting function and performed accounting related audits (Brink 1991). The internal auditor usually had some kinds of quality control function for example to verify that the accounting operations of the organization were performed correctly to instructions and standards.

According to Courtemanche, (1991). The external auditors continued to have a strong influence on the work and approach of internal audit, from the perspective of the task of the external auditors, being the assurance for reliable financial statements.

Towards 1900, the audit profession developed as more systematic approach and become more extensive. The association of professional auditors was established in the 16<sup>th</sup> century in Venice, Bologna and Mila. Prior of this, internal auditors were mostly state auditors who acted on behalf of the king and or state. During the 16<sup>th</sup> to 18<sup>th</sup> centuries the work area of audit expanded to include the transactions of business oriented society. The focus remained on fraud detection and

prevention of verifying each transaction with the supporting source documentation (Gupta and Ray 1992).

From the 1930 onwards the Securities and Exchange Commission (SEC) required firms to provide audited financial statements .if they wanted to be registered at the stock exchange (Gupta and Ray 1993).This increased the work for external audit firms and had consequences for their approach of work. Increasingly, the external firms worked with sample sizes and limited their detailed verification work to transactions .This change of approach by the external audit ors strengthened the establishment of internal audit function within firms in order to complete the detailed verification activities of transactions which were previously performed by the external audit firm. In that sense, the internal audit function could be seen as an extension to the work of the external auditor.

In Europe the first indications of an audit practice are found in the ancient Rome. Through hearings, verifications were made of record keepers and their financial accounts designed to prevent fraudulent acts (Sawyer 1996).

The origins of the more recent internal audit function can be traced to the 19<sup>th</sup> century US and UK railways (Spraa man 2001) and related development of accounting systems.

According to Ramamoorti (2003) internal auditing dates back to the Mesopotamian civilization around 4000.3500BC .Formal record keeping systems were introduced by organized businesses and governments to allay their concerns about incorrect accounting of receipts and disbursements and collecting taxes.

Furthermore the need for and indications of audits can be traced among other public finance systems in Babylonia, Greece, the Roman Empire and the city states of Italy all of which

developed a detailed system of checks and counter checks to prevent book keeping errors and inaccuracies as well as fraud and corruption.

He also suggests that the focus of internal audit was on the financial process and was very similar to what now is called financial audit.

In addition, internal auditors also investigated non financial data such as quantities of parts in short supply, adherence to schedules and the quality of products.

### **1.1.2 Theoretical background**

#### **Agency theory**

According to A. H. Millichamp and J.R. Taylor, (2008) Agency is the name given to the practice by which productive resources owned by one person or group are managed by another person or groups of persons, Agency theory is the recognition that inclination of agents such as directors or managers of the business is to act rather more in their own interests than the employers, the stakeholders. In the principle the Agency model assumes that no agents are trustworthy and if they can make themselves richer at the expense of their principals they will. The poor principals, so the argument goes, has no alternative but to compensate the agent well for their endeavors so that they will not be tempted to go into business for themselves using the principals assets to do so.(The Institute of Chartered Accountants, 2006)

#### **Contingency theory**

The goal of an audit is to test the reliability of the company's information, policies, practices and procedures. Government regulations require that certain organizations undergo independent financial audits but industry standards can mandate audits in other areas such as safety and

technology. Regardless of the audit subject, various factors impact companies' final results and contingency theory takes these factors into account during the audit process. (Nancy 2013)

Furthermore, the contingency theory of leadership and management states that there is no standard method by which businesses can be led, controlled and managed. Businesses and their functions depend on various external and internal factors. The functions of audits are themselves, types of businesses that are affected by various factors in the environment. The presence of such factors is why auditing can be managed by applying the contingency theory, with recognition that process and outcomes of audits are dependent on variable and contingent factors.

According to Draft (2012), contingency means one thing depends on other things and contingency theory means it depends. Audit functions are task oriented and can be loosely structured. The functions also can vary considerably, depending on the area of the company under audit and the type of the business model, so auditors must carefully manage their inspections and take variables into account to get the jobs done. The contingency theory also can be applied to an audit team's structure. Typically, audit team managers receive audit projects. They then create adhoc audit team for the projects, selecting auditors based on expertise and experience in the subject areas and on auditor availability, all of which add up to contingencies for any given audit project.

Audit teams use blend of structure and contingency to get output rolling quickly. The subject of auditing project can include such diverse areas as evaluation of production processes inspection of company accounts and assessment of compliance with industry standards.

Selecting auditors with specialized training or those who have a particular skill set in the subject area minimizes the learning curve and reduces opportunities for errors.

The quality and output of audits remain assured when audit teams use resources according to expertise and experience and when auditors are flexible and can adapt to process fluctuations.

(Davoren 1994)

### **Lending credibility theory**

Volosin (2007) lending credibility theory is similar to the agency theory and it states that audited financial statements can enhance stakeholder's faith in management's stewardship. The business world consists of different groups that are affected by, or participate in the financial reporting requirements of the regulatory agencies.

The research study was based on the contingency theory because businesses under go independent financial audits and take other factors into account during the audit process hence improving financial performance of the businesses.

### **1.1.3 Conceptual background**

Audit is a Latin word , meaning 'he hears ' our word audit is derived in this way since, In ancient times ,the accounts of an estate, domain or manor were checked by hearing them called out to those in authority by those who had compiled them.

According to American Accounting Association (AAA) Journal (2012) the organization of accounting professions define Auditing as a systematic process of objectively obtaining and evaluating evidence regarding assertions about economic actions and events to ascertain the degree of correspondence between those assertions and established criteria and communicate the results to interested users . The audited accounts must be published by the end of the financial year.

An auditor gets an understanding of the nature of the client's business and carries out general tests on the internal control system to find out which controls are in place and whether they are



operational. (Hoskisson, 2009) defines internal auditing as an appraisal or monitoring activity set up by management to review and report on the internal financial control system of the organization. Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve on the business's operations (Institute of Internal auditors 1999).

The scope of internal auditing within business is a broad and may involve topics such as business governance, risk management and management controls over: efficiency / effectiveness of operations (including safe guarding of assets), the reliability of financial and management reporting and compliance with laws and regulations in addition it may also involves conducting proactive fraud audits to identify potentially fraudulent acts : participating in fraud investigation under the direction of fraud investigation professionals and conducting post investigation fraud audits to identify control breakdowns & establish financial loss( internal auditing wiki pedia).

According to Richard L. Draft and Dorothy Marcic (2007) small businesses are growing in importance. Hundreds of small businesses are opened every month by people who have found themselves squeezed out of the corporation due to downsizing, who voluntarily leave the corporate world to be their own bosses, or who seek a slower pace and a healthier balance between work and family live.

Many small businesses are opened by women or minorities are opened by women or minorities who find limited opportunities for advancement in large corporations.

Business performance is a major concern these days due to importance of the global competition, one factor of this performance lies on the ethical and responsible behavior of its performers. But at the end of the 20<sup>th</sup> century, the Enron and world com scandals show that there was lack of control in businesses. [Bertin 2007]

Performance is the accomplishment of a given task measured against present known standards of accuracy, completeness, cost, and speed in contract. It is deemed to be the fulfillment of an obligation in a manner that releases the performer from all liabilities under the contract ([www.businessdictionary.com/definition/performance.html](http://www.businessdictionary.com/definition/performance.html)).

Performance sets general quality criteria for conducting an audit. The performance of the audit is also influenced by the need for auditors to exercise professional skepticism. The scope of audit function is not limited to independent audit. Internal auditing is another significant type of audit which involves conducting a systematic examination of the records, systems and procedures and operations of the business as a service to management under the allied concept of management audit, the performance of the management itself is appraised. [Kamal Gupta 2005].

Internal audit, traditionally developed as an audit on behalf of the management to ensure that the existing internal controls are adequate and effective, the financial and other records and reports show the results of operations accurately and promptly and each unit of the business follows the policies and procedures laid down by the top management, thus traditionally internal audit was primarily concerned with questions like whether the assets of the business were adequately safeguarded and properly accounted for, whether the accounting and other allied records were reliable, and whether the business procedures and policies were complied with. With significant emphasis on the detection of frauds and accuracy of financial records, the internal auditors were viewed as status quo oriented auditors of financial records and a somewhat unfortunate brother statutory auditor. As such he was mostly engaged in conducting routine checking of stock records, purchase invoices, cash receipts and payments, sales bills and other similar records and documents. (Kamal Gupta 2005)

The modern concept of internal auditing goes for beyond the traditional limits. Internal audit is no longer considered as a mere routine review of financial and other records by especially assigned staff. As the institute of internal auditors (2004) defines it internal auditing is an independent and objective assurance and consulting activity designed to add value and improve on the business's operations. It helps the business to accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance process.

Further IIA states that internal audit activities are performed by persons within or outside the organization.

In recent years, businesses have grown enormously in size and operations .Many of them employs thousands of persons and conduct operations from various locations. It has therefore become necessary for the managements of such businesses to have a team of specialists to review the procedures and operations of various units and report cases of non compliance, inefficiency and lack of control, so that necessary corrective actions can be taken. The task cannot obviously be left to the statutory auditors whose main objective is to report whether or not the financial statements reflect a true and a fair view of the working results and financial position of an enterprise. Internal auditing has therefore become a specialized service requiring not only expertise in accounting but also in organizational behavior and in functional areas of management. (Kamal Gupta 2005).

In its modern sense, an audit is a process ( carried out by suitably qualified auditors) whereby the accounts of business entities, Including limited companies charities, trust and professional firms, are subjected to scrutiny in such detail as will enable the auditors to form an opinion as to their truth and fairness. This opinion is then embodied in an ``audit report'', addressed to those parties

who commissioned the audit, or to whom the auditors are responsible under statute. (Emile woolf 1978).

In the past internal auditors have been defined as auditors working for the organization that they were auditing. Internal auditors were employed by the organization such a bank hospital, city government or industrial company.

However in recent years, many professional services firms are providing internal audit services to the business community.

Therefore, internal auditors may now be employed by either the organization.

They are auditing or an independent professional services firm.

Many corporations believe that they gain expertise and improve control over audit costs when the internal audit function is out sourced to an external audit firm conversely, many companies believe that in – house internal audit function is better aligned with the company goals and objectives and auditors gain more experience and expertise with the company’s organization and business. Currently we are seeing more firms implementing a “Co-sourcing ‘strategy where the company retains an in house’” internal audit department augmented with auditors from an outside firm. This strategy allows the company to have a core audit group dedicated to the company with specialized “Institutional Knowledge” in the company policy procedure and strategy yet the company can employ the expert industry and audit knowledge of a professional services firm directly to specific engagements or projects. (Louwesrsetal 2011).

These ranged from under 200 employees for manufacturing firm to over E50000 turn over (in 1971) for retailing and up to five vehicles or less for road transport. So many definitions clearly cause practical problems the more definitions based on financial criteria suffer from inherent problems related to inflation and currency translation.

The UK companies act has special less stringent reporting requirements for small firms using the following definitions maximum annual turnover of E2.8 million, Maximum annual balance sheet total of E1.4 million and maximum number of employees of 50.

Being small size, is not just about the size, defined in simple statistical terms, small firms also have important defining characteristics such as market influence independence and personal influence.

Small firms start to make managerial appointments when they have some 10-20 employees and at this point they start to take on the appearance of more formal structure (Atkinson and meager, 1994).

Nevertheless, this third point is the key to definition of the real small firm the one with potentials the one that economists cannot understand the one that is so different from the firm. Essentially the real small firm can be described as having "two arms two legs and a giant ego. In other worlds, it is an extension of person, be he/she owner - manager is entrepreneur to the firm. The personality of the manger is imprinted on the way it operates and personal risks them and their family face if the firm fails influences how business decisions are made.

In addition, the internet has opened new avenue for a small business formation. The huge wave of d.o com start ups in the late 1990's was driven by dreams of wealth and by the desire of people to get out of big corporations and start something new and exciting.

Today environment for small business is highly complicated. Advances in technology, globalization, government regulation and increasing customer demands require that even the smallest of business have solid management expertise. However, small companies sometimes have difficulty developing the managerial dexterity need to survive in a turbulent environment on one survey on trends and future development in small business found that nearly half of

respondents saw inadequate management skills as a threat to their companies, as compared to less than 25 percent of larger organizations.

Managers in small business tend to emphasize roles different from those of managers in larger corporations. Managers in small companies often see their most important roles as spokes persons because they must promote the small growing company to the outside world.

The entrepreneur role is important in small businesses because managers have to be creative and help their organization develop new ideas to remain competitive and professional judgment throughout the audit process. It contains five elements that is to say reasonable assurance, planning and supervision, materiality, risk assessment and audit evidence.

#### **1.1.4 Contextual background**

An internal auditor may be assigned to evaluate the cost effectiveness of the company's policy to lease, rather than to purchase heavy equipments. The internal auditors rely a great deal on financial and managerial models of efficiency and economy (louwers' etal 2011).

In recent years, the responsibility of the internal auditor to identify and detect fraud has been of great important in most countries.

Assuming the increasing significance in the context of some major frauds in high profile companies and their damaging effects on the capital markets. It is recognized that internal auditors are responsible for assisting the deterrence of fraud by examining and evaluating the adequacy and effectiveness of the internal control system, commensurate with the extent of the potential exposure/ risk in the organization's operations. Adequate control is a principle mechanism for deterring fraud and limiting its exposure and the primary responsibility for establishing and maintaining control rests with management. (Kamal Gupta 2005).

Internal auditing is primarily concerned with reviewing all the functions of management such as planning, organizing, controlling, staffing and leading in order to attain organizational effectiveness (Rainey 2006) hence improving on the financial performance.

According to Collier et al., (1991) Internal auditing helps the small scale businesses to accomplish objectives by bringing up a systematic disciplined approach, to evaluate and improve the effectiveness of risk management, control and governance process leading to good financial performance. It also acts as an important link between organizations and reporting process of corporation (Reynolds 2000).

Internal auditing has become increasingly important as more corporations are looking beyond their own country's financial performance so as to compete internationally. High quality internal auditing is the key to financial performance of any corporation and it is the foundation of social and economic progress and this helps to review the organization, operations as a service to management (Agoula 2002).

## **1.2 Problem statement.**

Internal auditing activity is directed at evaluating internal control. Under the COSO framework, internal control is broadly defined as a process affected by an entity's board of directors, management and other personnel designed to provide reasonable assurance regarding to achievement of the core objectives for which all businesses strive such as effectiveness and efficiency of operations, reliability of financial and management reporting, compliance with laws and regulations and safeguarding of assets (Amundo and Inanga 2009.)

Small scale business owners set goals and objectives to be achieved through the use of internal control measures or systems. It comprises the control environment and control procedures adopted by the directors and management of an entity to assist in achieving their objective of

ensuring, as far as practicable, the orderly and efficient conduct of its business including adherence to internal policies, Safe guarding of assets, the prevention and detection of fraud and errors the accuracy and completeness of the accounting records, and the timely preparation of reliable financial information (Emile woolf 1978)

Furthermore internal auditing is an independent, objectives assurance and consulting activity that adds value to and improves an organizations operation. It helps an organizations accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management control and governance process. Internal auditors are employed by organizations such as banks, hospitals, city governments and industrial companies. (Millichamp and taylor ( 2008)

Sarbanes –oxley (2002) required an audit of the effectiveness of internal control over financial reporting for public companies because it is an integrated part of the financial statement audit. In essence, the public accounting firm issues two opinions one on the entity’s financial statements and one on the entity’ internal control. The other primary reason for evaluating an entity’s internal control is to assess the risk of material misstatement to give the auditors a basis for planning the audit and determining the nature, timing and extent of audit procedures for the substantive audit plan.

However, there is a problem of materiality, it’s the magnitude of omission or misstatement of accounting information that, in the light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the omission or misstatement, it may be due to error or fraud. Materiality is an



account or fact that would affect decisions made by users relying on the financial statements and this affects the performance of the small scale business (William F. Messier 2000)

Furthermore there are still other cases of misappropriation of funds, mismanagement such as in adequate supervision or monitoring of remote locations and abuse of offices that leads to poor performance and loss of profits. Inadequate record keeping for assets susceptible to theft hence losing assets in small scale business (Auditor general's report 2006).Therefore the researcher intended to examine the contribution of internal auditing on the financial performance of small scale businesses in Katwe-Butego Division.

### **1.3 General objective**

To examine the contribution of internal auditing on the financial performance of small scale business in Katwe-Butego Division.

### **1.4 Specific objectives**

1. To determine the contribution of financial audit on the financial performance of small scale business in Katwe-Butego Division.
2. To find out the contribution information system audit on the financial performance of small scale businesses in Katwe-Butego Division.
3. To determine the contribution of compliance audit on the financial performance of small scale business in Katwe-Butego Division.

### **1.5 Research questions**

1. What is the contribution of financial audit on the financial performance of small scale businesses in Katwe-Butego Division?

2. What is the contribution of information system audit on the financial performance of small scale business in Katwe-Butego Division?
3. What is the contribution of compliance audit on the financial performance of small scale businesses in Katwe-Butego Division?

## **1.6 Scope of the study.**

### **1.6.1 Geographical scope**

The study was conducted in Katwe Butego Division Masaka Municipality found in Masaka district along Elgin Street, Katwe road and Masaka road. It is surrounded by different businesses such as hotels like Brovard, Maria, schools and hospitals.

Masaka district is situated about 37 kilometers away from the equator towards the South and lies between 0 degrees 25 South and 34 degrees East, having an average attitude of 1150m above the sea level.

### **1.6.2 Content scope.**

The study was based on the contribution of internal auditing on the performance of small scale businesses in Katwe-Butego Division Masaka Municipality. This include the contribution of financial audit, information system audit, compliance audit, operational audit, follow up, and investigation. The researcher based the first three types that is to say financial, information system and compliance. This was because such internal auditing activities were commonly used by the small scale business in Katwe Butego Division. Every organization prepares financial statements that need to be audited and the technology is developed organizations use computers.

### **1.6.3 Time scope**

The research study covered a period between 2014 to 2017. The time scope is up to date because different books and journals about the contribution of Internal auditing on the financial performance of small scale businesses were produced up to date This gave appropriate time for the researcher to get more information which was relevant to the study. .

### **1.7 Significance of the study**

The study will be of great important to the people of Katwe-Butego and Uganda as a whole by putting in place the appropriate remedies to solve the problem.

The findings will be of great importance to the policy makers and implementers in KatweButego such as schools like the board of governors, who are the policy makers of rules and regulations to guide the employee's behavior must especially the bursars.

The study will guide other businesses in appreciating the aim, results of auditing and business performance.

The research will add knowledge and ideas to future researchers and students of higher learning.

It will help the scholars to appreciate and enhance their knowledge of internal audit so as to adhere to the professional ethics as required by the IAS.

The research will give shareholders an accounting on how their investment are performing

The study will also help the shareholders to appreciate the contribution of internal audit as one of the important managerial control systems in an organization required to safe guard their interest.

### **1.8 Justification of the study**

The study is the university's requirement for award of Bachelor's degree in Business administration and management at Uganda Martyrs University.

In the Auditors general’s report (2006) it showed that internal auditing is done but a lot of government funds are lost due to embezzlement, misappropriate and lack of accountability

As the business grows bigger also the number of transactions also grows tremendously and this calls for new controls to enable such a company to cope up with the need for expert knowledge in the auditing (Aggrey, 2000).

### 1.9 Conceptual frame work

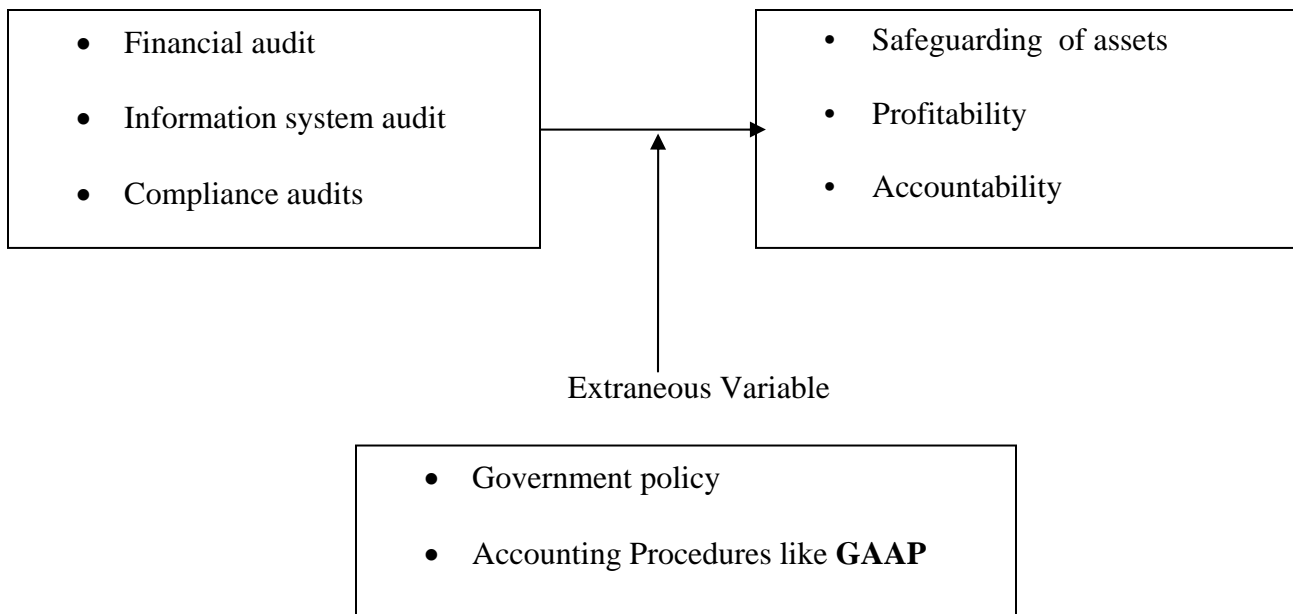
Conceptual framework of internal auditing and financial performance of small scale business.

Independent Variable

Dependent Variable

**Internal auditing**

**Performance of small scale businesses**



Source Designed by the researcher with help of louwersetal (2011)

Here the independent Variable is internal auditing and the dependent Variable is the financial performance of small scale businesses. Financial audits help to safeguard assets, profitability and improve accountability for the efficient and economical use of resources and achievement of program goals hence leading to financial the performance of small scale businesses. Although Internal auditing services such as information system, compliance help to improved accountability, safe guard assets, extraneous variables such as government policies, accounting procedures like GAAP also intervene.

### **1.10 Conclusion**

The chapter identifies the introduction, background, problem statement, general objective, specific objectives, Research questions, scope of the study, and significance of the study. Justification of the study, limitation of the study and conceptual frame work and the next chapter is literatures review

## CHAPTER TWO

### LITERATURE REVIEW.

#### **2.0 Introduction**

Literature review examined different scholars on the contribution of internal auditing on Financial performance and the specific variables or objectives.

#### **2.1 Actual review**

##### **2.2.1 Financial audit and financial performance**

Financial audit is an audit of financial statements enables the auditors to express an opinion whether the financial statements prepared , in all material respects ,in accordance with in identified financial reporting frame work .(Paape 2007)

Financial audit is conducted to provide an opinion whether financial statements the information being verified are stated in accordance with specific criteria normally the criteria are international accounting standards although auditors may conduct audits of financial statements prepared using cash basis or some other basis of accounting appropriate for the business. In providing an opinion whether financial statements are fairly stated in accordance with accounting standards the auditors gathers evidence to determine whether the statements contain material errors or other misstatements. (Arens el at 2012)

The audit opinion is intended to provide reasonable assurance but not absolute assurance that financial statements are presented fairly in all material respects and give a true and fair view in accordance with the financial reporting framework. The purpose of the audit is to provide an objective independent examination of financial statements which increase the value and credibility of financial statements produced by the management thus increasing the user

confidence in the financial statements, reduce investor risk and consequently reduce the cost of capital of the preparer of financial statements.([https://en.wikipedia.org/wiki/financial\\_audit](https://en.wikipedia.org/wiki/financial_audit))

Financial audit exists to add credibility to the implied assertions by an organization's management that its financial statements fairly represent the organization's position and performance to the firm's stake holder. The principle stake holder of a company are typically its stakeholders that other parties such as tax authorities, banks regulators, suppliers, customers and employees may have also an interest in knowing that the financial statements are presented fairly in all material aspects. An auditor is not designed to provide absolute assurance, being based on sampling and not testing all transactions and balances rather it designed to reduce the risk of material financial statements misstatements whether caused by fraud or error. Audits exists because they had value through easing the cost of information asymmetry and reducing information not because they are required by the law (The institute of chartered accountants 2011)

According to Vincent M O Reilly etal (1998) financial audit seeks evidence about assertions related mainly to financial information, usually contained in a set of financial statements. Generally the information will be used by parties other than the management of the entity that prepared it. Sometimes, however the information is intended to be used primarily by management for internal decision making purposes. It may include non financial as well as financial data.

However financial audits are associated with independent auditors whose work results in an opinion on financial statements, both internal auditors and government auditors also perform financial audits, often in conjunction with compliance audit.

### **2.2.2 Compliance audit**

According to Patrick J M C Donnell(1998) compliance audits are intended to determine whether an entity has complied with specified policies , procedures, laws, regulations or contracts that affect operations or reports.

Furthermore laws and government regulations play an integral part in an entity's operations and failure to comply with them may affect its financial statements. Management is responsible for ensuring that the entity complies with applicable laws and regulations.

According to section 316, the auditors assess the risk of the material misstatement of financial statements due to fraud and consider that the assessment in designing audit procedures to be performed in order to ensure an effective risk assessment.

According to paape (2007) compliance audit is an audit carried out to assess whether the organization adheres to certain specific requirements of policy, procedures, standards, laws and governmental regulations. From the organizational perspective combining the functions has the clear benefit of reducing administrative burden on the CEO or other senior managers to whom the functions would report.

This would make more efficient use of board members' time by stream line reporting to the audit and even a great benefit may come from the improvement in organizational governance by enabling the board members to move efficiently when fulfilling their duties for oversight of ethics and compliance as well as overall risk management and internal control (R. Walker 2009)

### **2.2.3 Information system audits and financial performance**

Change in technology requires a change in controls so as to run the company effectively. Advent of computerized system and the new systems necessitated changes in control to adapt to the working environment conditions. This helps to produce reports and management information quickly hence leading to improved financial performance of the businesses (Hayes 2005)



Even the smallest organizations have computers now and use computerized accounting package to maintain their accounts, they help to control the information being input into the system for example; they require a code number to be input thus aiding posting to the correct accounts(Millichamp 2008)

However computer information systems can also become a problem for both auditors and management if they are not properly controlled, for example inadequate computer systems can lead to misleading information being produced and can encourage fraudsters (Millichamp 2008)

## **CHAPTER THREE**

### **METHODOLOGY**

#### **3.0 Introduction**

This chapter presents the description of the methodology that employed in the study. Methodology was a detailed procedure used to answer the research. It included a description of research design, sampling techniques, study population, area of the study, sampling size and selection, methods of data collection, data analysis and management, quality control methods ethical consideration and conclusion.

#### **3.1 Research design**

According to Oso and Onen (2009), research design is a selection that the researcher intends to follow the plan or strategy for conducting the research.

The study was conducted basing on case study designs that connect qualitative and quantitative approach.

Hayes (1999) defines quantitative data as data obtained from respondents through use of questionnaires, interview guides and observations. During the study, the researcher relied on random sampling and structured data collection instruments that fitted diverse experience and response categories. This method of the study helped the researcher to produce results that are easy to summarize, compare and generalize and also to capture the opinions of the respondents. Depending on the research questions, participants were randomly assigned to different treatments. The researcher collected data on respondents and situational characteristics in order to statistically control their influence on the dependent, outcome variable.

Kyla (2003) defines the qualitative data as the data obtained from the existing literature of different authors and scholars. It includes textbooks, notes, reports and others this helped the

researcher to integrate findings with existing literature about the study problem. This design was good for the study because it generates quick self reports from the participants under the study. Also the response that was generated from participants in a study conducted under this type of design portrayed picture that was adequately generalizable for the entire population.

### 3.3 Area of the study

The study area was businesses business located within Katwe- Butego Division in Masaka Municipality. Masaka Municipality is made up of three divisions and these are Katwe-Butego, Nyendo Ssenyange and Kimaanya Kyabakuza found in Central Uganda. Most of the businesses are located in Kirumba industrial area which is boarded by Nyendo Ssenyange Division.

### 3.4 Study population

The study was conducted within businesses that carryout internal auditing in Katwe Butego division Masaka Municipality such businesses with a target population of 101 respondents.

**Table 1**

<b>Business</b>	<b>Number</b>	<b>Sample</b>
Primary schools	50	43
Secondary schools	20	16
Clinics	10	9
Maize mills	15	10
Supermarkets	6	2
<b>Total</b>	<b>101</b>	<b>80</b>

### 3.5 Sample size and selection

Ngechu (2004) underscores the importance of selecting a representative sample through making a sampling frame. From the population frame the required number of subject, respondents, and elements were selected in order to make a sample .The sample included 101 businesses in Katwe Butego. The study selected 80 respondents from the targeted population of 101businesses in Katwe Butego Division .The businesses were selected in terms of their size, the big, the medium and the small. Using the Morgan formula.

$$S = \frac{X^2NP(1-P)}{D^2(N-1) + X^2P(1-P)} ;$$

Whereby;

X = Standard confidence level (1.96), N = Population size,

P = Standard population proportion (0.5), S = required sample size, and

D = Degree of accuracy (expressed as a proportion of 0.05) meaning the margin of error.

### 3.6 Sampling techniques

In the study, the researcher used a simple purposive sampling technique among the Katwe Butego business organizations from auditing department, management and accounting department. This helped the researcher to get the data which is applicable to the study, relevant and accurate .It also reduced on time wastage because the respondents had knowledge about internal auditing.

**Table 2**

Category people	Expected respondents
Cashiers	25
Auditors	10
Accountants	30
Owners	15
Total	80

**Source: Primary data 2017**

From the data above, as represented in the table, it reveals that the researcher obtained data from 25 cashiers, 10 auditors, 30 accountants and lastly 15 owners. This means that the researcher obtained data from the relevant population (respondents) making the data collected valid and reliable.

**3.7 Methods and instruments of data collection**

**Primary data**

Primary data provided firsthand information directly from the respondents through questionnaires, interviews and discussions with relevant stake holders to the study and observation .Much of the conclusions were based on this source. Primary data was collected from the respondents using self-administered questionnaires which created anonymity leading to more valid responses as well as allowing respondents to fill them at their convenience. The questionnaires were designed according to the objectives and study variables

The researcher used questionnaires that were both open and closed ended questions. The researcher used structures questionnaires formulated and directed to the sample subject. The

reason why the questionnaires were used for this study was because it intended to cover a number of respondents in short time and it was less expensive for the researcher (Amin 2005). The close ended questions involved questions which required answers limited within a scope which involved yes and No answers. The open ended questions involved questions that required the respondents to give their own opinions.

The following are reasons why the researcher used questionnaires.

The questionnaires gave respondents ample time to think and express themselves and quite a lot of information was collected in relatively short period of time.

The researcher broadly utilized questionnaires as a sampling technique since most times numerous individuals feel anxious to tell the truth during face to face interviews .The researcher was in good position to get specific and reliable data regarding the research topic in question.

The questionnaires saved time for the respondents because the questions were answered at the respondents, pace after the working hours hence no disturbance of the respondent's work

The researcher also used interviews when collecting the necessary data. The interviewing method was used because it involved face to face exchange of ideas which helped the research to get first-hand information and immediate feedback thus saving time for the study.

The interview guide helped the researcher to express her view on the respondents, responses to analyze the response properly.

There was direct interaction between the researcher and the respondent's .This helped the researcher get more clarification from the respondents to understand the insight in the response clearly

### **3.8 Data process, management and analysis**

The researcher first sought permission from the respondents then the researcher started to collect data from the respondents through interviewing and use of questionnaires. The research was conducted in the morning when the workers were still fresh and this helped the researcher to get to answers which are not biased

The collected data from the questionnaires was edited, coded, tabulated and analyzed and there after simple descriptive statistics, frequencies and percentages were computed to help in the discussion of findings and was processed for further scrutiny and checking of omissions through classification and updating.

The research data was analyzed by both quantitative and qualitative techniques. Qualitative techniques involved factual and logical explanation and interpretation of the findings. Qualitative data was analyzed in the field as it was being collected using coding sheets. While quantitative was analyzed by use of computer programs like Microsoft word and Microsoft excel. Quantitative technique on the other hand involved the use of descriptive statistics such as percentages and averages .Relevant tables were also used to present data. The use of percentage, averages and relevant tables made the presentation and analysis of data more clean and easy to all. The readers can easily make comparisons and quickly grasp the analysis and conclusion that was made.

### **3.9 Quality control methods**

#### **3.9.1 Reliability**

For the reliability of the findings, the researcher used pilot testing, pre-test and re-test technique. For pre-test ,the questionnaires were sent to the respondents at first and then collected after sometimes such as a week another questionnaire was formulated in a different way and sent to

the same respondents .Reliability ensured consistency of measurement or degree to which an instrument produces the same response every time.

Reliability is based on consistency of observation and replication or results. The measures relating to internal reliability are designed to ensure a maximum that other researchers using the same data would come to similar conclusions, those relating to the external reliability are designed to ensure that a third researcher following the same approach would get the same results by observing similar environment (Gagnon, 2005).

### **3.9.2 Validity**

According to Gagnon, (2005) validity to be confirmed, the research must meet several criteria. The first point to avoid is that as it is not anonymous in direct observations, it is possible that a person observed change in its behavior because he knows that he is observed knowing to be sure that it was not the case we made everything to do it, the diversity interviews, crosschecking data sources and duration of the research allowed us to reduce this bias. It also requires that the observed reality is a construct the mind as a collection of concrete phenomena.

Validity is the ability to produce findings that are in agreement with theoretical or conceptual values. In measuring the validity of these findings, the researcher used content validity because it focuses upon the extent to which the content of the instrument corresponds to the content of the theoretical concept.

### **3.10 Ethical consideration**

Before commencing the research, an introductory letter from the university was sought and the purpose of the study explained to the potential respondents to avoid inconveniences and misunderstandings about the purpose of the study.



The information gathered from the respondents was kept with maximum confidentiality or with due respect in order to recognize the dignity of respondents by not mentioning their names or any form of identification thus keeping their privacy.

### **3.11 Limitations of the study**

Some respondents never had enough time because they were busy and this affected the researcher because she never got enough information for the study.

Time limit, some respondents did not honor their appointments which necessitated rescheduling the appointments for the future and time. This made it impossible for the researcher to complete the study within the stated time.

Some of the respondents were not ready to give out the information and this affected the researcher because she did not have right and relevant information since some respondents hid important information that was relevant to the area of study.

The researcher had limited funds, such as transport feeding and stationary however, the researcher requested for some assistance from the family and friends in order to successfully complete the study.

### **3 1 2 Conclusion**

This chapter has identified the study's methodological tools and approaches used by the researcher and the next is chapter four.

## CHAPTER FOUR

### DATA PRESENTATION AND DISCUSSION OF FINDINGS.

#### 4.0 Introduction

This chapter presents the output of data analysis. The presentations are in form of tables and statements. The presentation is according to the objectives of the study. The methods of analyzed data were qualitative and quantitative, the qualitative was describing and elaborating on the responses of the respondents and the quantitative method involves the computation of percentages graphs and tables.

#### 4.1 Gender of respondents

The study examines and describes the gender details of respondents in this study and a detail of their respective gender is presented in the table below.

**Table 3. Gender characteristics of respondents.**

<b>Gender</b>	<b>Frequency</b>	<b>Percentage</b>
Male	35	56.2
Female	45	43.8
<b>Total</b>	<b>80</b>	<b>100</b>

**Source; primary data 2017**

The finding above reveals that 56.2% of the respondents were female and 43.8% were male. This could indicate that there are still low levels of employment of males in the small scale businesses. The findings represent the view of the two sex groups about financial audits and financial performance of small scale businesses. This was necessary for the study to get a balanced picture of the respondent's views about the contribution of financial audit. This might

be concluded that majority of females participate in the business most especially in finance department because they are more trust worthy compared to males

#### 4.2 Education level of the respondents

Details about the education levels of respondents were obtained and the results are revealed in the table below.

**Table4: Showing the Educational level of respondents**

Qualification	Frequency	Percentage (%)
Diploma	15	18.8
Bachelor	18	22.5
Masters	2	2.5
Certificate	35	43.8
Others	10	12.5
<b>Total</b>	<b>80</b>	<b>100</b>

**Source: Primary data, 2017.**

In the above table, it can be revealed that majority of respondents show that they hold certificates by 43.8% followed by bachelor's holder 22.5%, diploma, 18.8%, others 12.5% and master's degree 2.5% respectively. This means that the respondents are adequately qualified persons academically.

#### 4.3 Description of the positions of the respondents in the business

The study sought and obtained details about the positions held by the respondents in the business for purposes of understanding their role in the variables of study. Details of the respondents and their positions are shown in the table below.

**Table5: Showing the positions of the respondents in the businesses**

<b>Position held</b>	<b>Frequency</b>	<b>Percentage (%)</b>
Internal auditor	4	5
Chief internal auditor	5	6.3
Accountant	38	47.5
Finance manager	25	31.3
Team manager	8	10
<b>Total</b>	<b>80</b>	<b>100</b>

**Source: Primary data, 2017**

The analysis results in the table above shows that majority of respondents in this study are accountants with 47.5%, finance manager with 31.3%, team manager with 10%, chief internal auditor with 6.3%, and internal auditor with 5% respectively. From the above description, it can be revealed that the majority of the respondents in this study are those directly responsible for or directly involved in the implementation of the internal control system. Therefore their responses are deemed to reflect with what actually takes place in their businesses.

#### **4.4 Description of age groups of respondents**

The study obtained about the age group of the respondents for purposes of understanding their age and possibly the experience they possess in their respective positions. Details of the findings are shown in the table below.

**Table 6: Showing the age groups of respondents**

<b>Age group</b>	<b>Frequency</b>	<b>Percentage (%)</b>
20-33 years	30	37.5
30-40 years	28	35
40-50 years	15	18.8
50-60 years	7	8.8
Above 60 years	0	0
<b>Total</b>	<b>80</b>	<b>100</b>

**Source: Primary data, 2017**

From the description above it is clearly evident that the majority of the respondents are in the age bracket of between 20-30years, followed by 30-40years, 40-50years 50-60years and above 60 years in their orders of 37.5%, 35%, 18.8%, 8.8%and 0% respectively. It can therefore be concluded that the majority of the respondents are in the most productive age brackets of their life and are reasonably experienced.

#### **4.5 level of working experience**

The study investigated the length of period in years served by the respondents in the business and the findings are presented in the table below.

**Table7: Showing the level of working experience of the respondents**

<b>Experience</b>	<b>Frequency</b>	<b>Percentage (%)</b>
1-3 years	45	56.3
4-6 years	20	25
7-9 years	11	13.8
Above 10 years	4	4
<b>Total</b>	<b>80</b>	<b>100</b>

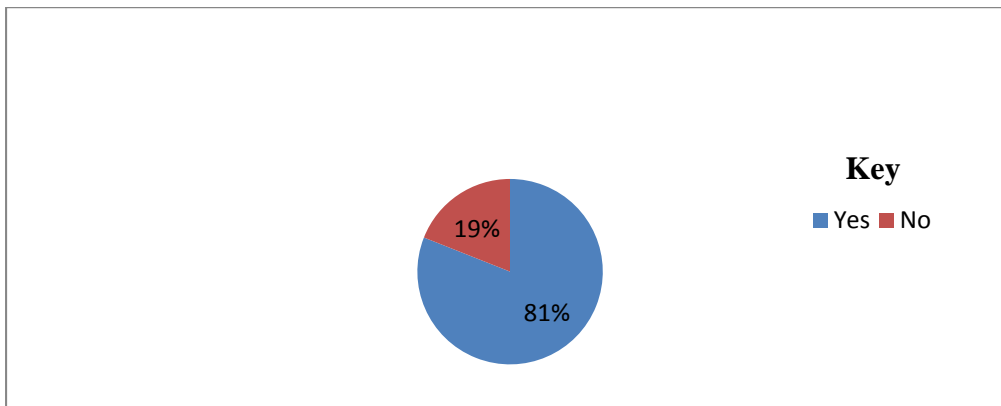
**Source: Primary data, 2017**

In the table above it can be revealed that majority of the respondents have worked in the organization for the period of 1-3years(45) ,followed by 4-6 years (20) , then 7-9 years (11) and lastly over 10 years(4). These represent 56.3%, 25%, 13.8% and 5% respectively. This could also show that majority of the respondents have worked in the business for less than 10 year.

**4.6 Number of workers in the business.**

During the study the researcher investigated on the number of workers in the business. The study was carried out below 20worker and over 20.The results were as follow.

**Figure 1: a pie chart showing the numbers of workers in the business**



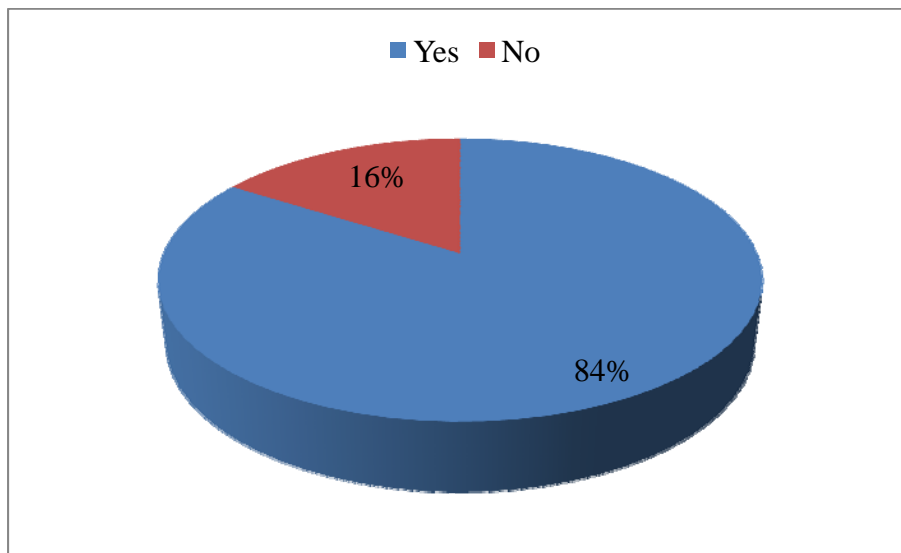
**Source: Primary data, 2017**

In the figure above shows that majority of the respondents 65 (81%) agreed that the business had employees above 20 workers and below 20 workers, the respondents were 15 (19%). The business employs over 20 workers because they perform a number of activities such as accountancy, production and operation in order to improve on the financial performance of the businesses.

**4.7 Financial audit and financial performance of the businesses**

During the study the researcher investigated whether financial audit was carried out by the businesses in Katwe Butego Division Masaka Municipality. The study was carried out on the contribution .for doing this the researcher wanted to know the contributions of financial audit in the businesses in Katwe Butego Division Masaka Municipality. The results were as below.

**Figure 2: a pie chart to show whether financial audit is practiced in the business**



**Source: Primary data, 2017**

In the figure above shows that the majority of the respondents 67 (84%) agreed that the financial audit contributes to the financial performance of the businesses in Katwe-Butego Division Masaka Municipality and 13 (16%) disagrees with it. It was revealed that financial audit was practiced and the following contributions were given by the respondents such as it helps the business to assess its current performance and thus serves as a basis for planning for the future, enables the business to control high cases of fraud which retards financial performance ,enables the business to carry out proper budgeting, helps in keeping up to date books of accounting, provides information to the management, allocate finance effectively, evaluate performance to know whether the business is making profits or losses, promotes eagerness of all workers concerned with finances in the business, helps in detecting fraud, errors, preparing standard financial reports, provides suggestions for restricting internal control systems , ensures compliance with accounting guide and standards, financial audit reports are relied on to suggest investment decision , it also gives the opinion of the auditor to the management to identify areas of improvement, it ensures that all records are accurate and reliable , ensures record keeping and references, improve on workers performance, trains workers on how to present reports and to be trustworthy, accountability purposes, monitor financial activities of the business and accountability and these were in line with what was said by Posthuma (2003) when he said that financial audits are essential because they are proactive and emphasize quality.

However, there are some respondents who said that their organization do not carry out financial audit because the business is not getting a lot in terms of profits that is why they do not carry out financial audit since it requires a lot of money to be paid for the practice and others said that the businesses are small and financial audit is not necessary.



#### 4.7.1 How often does your business carry out financial audit?

**Table 8: Showing the times the businesses carry out financial audit**

<b>Number of times</b>	<b>Frequency</b>	<b>Percentage (%)</b>
Once a week	6	9
Monthly	32	47
Twice	0	0
Quarterly	15	22
Annually	15	22
<b>Total</b>	<b>68</b>	<b>100</b>

*Source: Primary data, 2017*

From the above data presented in the table, it reveals that majority of the respondents mentioned that the businesses carry out financial audit monthly 47%, quarterly 22%, annually 22% and lastly once a week by 9%. This means that most of the financial audit activities is done monthly.

#### 4.7.2 Methods used by the businesses when carrying out financial audit

The researcher managed to collect data by on the methods used the businesses when carrying out financial audit on the financial performance.

The collected data was analyzed and presented in the table as below.

**Table 9: Showing methods used by businesses when carrying out financial audit on the financial performance.**

<b>Method</b>	<b>Frequency</b>	<b>Percentage (%)</b>
<b>Posting checking</b>	<b>5</b>	<b>7</b>
<b>Bank reconciliation</b>	<b>33</b>	<b>49</b>
<b>Inspection</b>	<b>16</b>	<b>24</b>
<b>Confirmation</b>	<b>2</b>	<b>3</b>
<b>Costing checking</b>	<b>5</b>	<b>7</b>
<b>Observation</b>	<b>0</b>	<b>0</b>
<b>Inquiry</b>	<b>0</b>	<b>0</b>
<b>Physical examination</b>	<b>7</b>	<b>10</b>
<b>Total</b>	<b>68</b>	<b>100</b>

*Source: Primary data, 2017*

From the table above ,it is revealed that majority of the respondents chose bank reconciliation as the most used method 33(49%), followed by inspection 16 (24%),physical examination 7 (10), posting checking and costing checking have the same 5(7%),confirmation 2(3%), lastly observation and inquiry have the same 0(0%).

#### **4.7.3 Challenges in carrying out financial audit.**

The respondents were able to give out the following challenges they face when carrying out financial audit.

**Table10: Showing the challenges faced when carrying out financial audit**

Challenges	Frequency	Percentage
Inadequate information given to the financial auditors from the management.	3	4.4
Improper book keeping	8	11.8
Huge allowances given to auditors.	10	14.7
Un intention error	2	2.9
Expensive	20	29.4
Inadequate knowledge	11	16.2
Un cooperative staff	6	8.8
Incomplete transactions	3	4.4
Employee transfer	4	5.9
Some important information is hidden by the accountants.	1	1.5
Total	68	100

*Source: Primary data, 2017*

From the table above, It was revealed that majority of the respondents pointed out expensive as the most challenge in carrying out financial audit, 20(29.4%) followed by inadequate knowledge 11(16.2%), huge allowances given to the auditors 10(14.7%), improper book keeping 8(11.8%) un cooperative staff 6(8.8%), employee transfer 4(5.9%), inadequate information given to the financial auditors from the management and incomplete transactions have the same 3(4.4%), un intension error 2(2.9%) and lastly some important information is hidden by the accountants

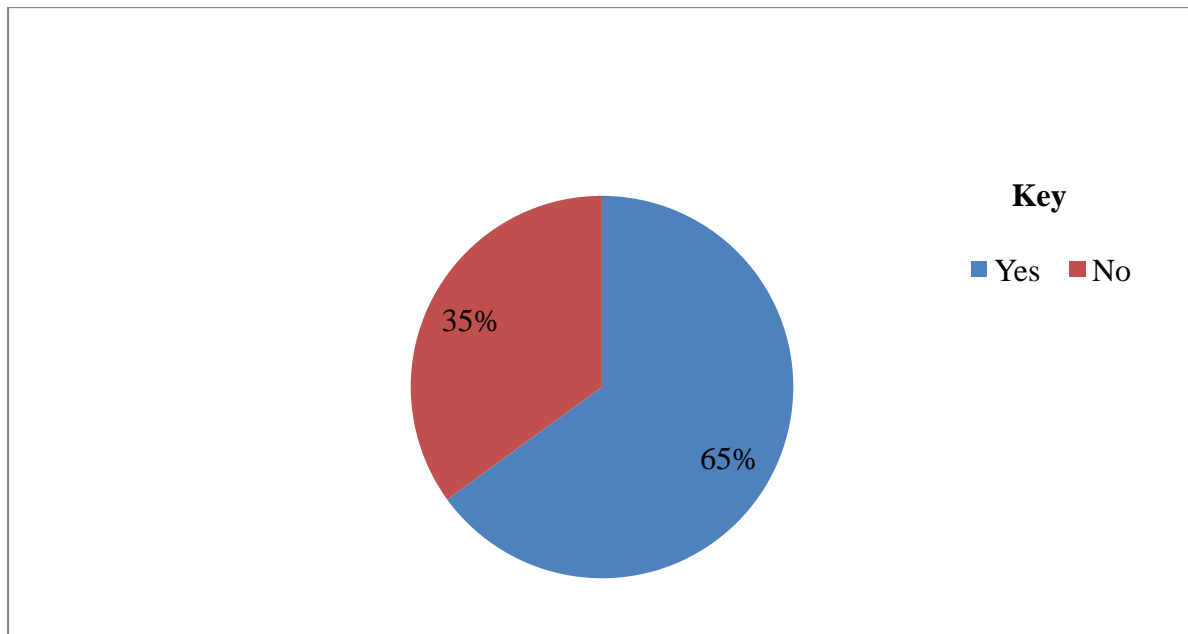
1(1.5%) which affect the financial performance of the businesses in Katwe Butego Division Masaka Municipality.

#### 4.8 Information system audit and financial performance of the business

During the study the researcher investigated whether information system audit was carried out by the businesses within Katwe-Butego Division Masaka municipality basing on the study was carried out the businesses. On doing this the researcher wanted to know the contributions of information system audit in the organization in Katwe-Butego Division Masaka Municipality.

The results were as follow

**Figure 3: Below shows whether information system audit is carried out in the business**



*Source: Primary data, 2017*

In the figure- show that the majority of the respondents 52(65%) agreed that information system audit is practiced in the business and 28(35%) disagreed with it. It revealed that information system audit contributes to the financial performance of the business and the following were the contributions suggested by the respondents, it helps to prepare reports in time, keep the records

safe, help to detect error and fraud, Verification of the right information system soft ware, ensures that information security is maintained, helps to find out the right person who access the business information, eases audit work. helps in maintaining of proper financial information, avoids losing of the data, improves communication channel, it is quick and it helps the user department to assess whether their business's financial statements are consistent with regard to GAAP, minimizes the space for keeping the information, reduces duplication of information, data is always reliable and it minimizes manual labour.

However, there are some respondents who disagreed that they do not practice that information system audit because they lack an outstanding information system, it is costly, needs qualified personnel, ignorance about its importance not yet focused on, some said that they do not have computers and others said that they use manual system.

#### **Challenges of carrying out information system audit**

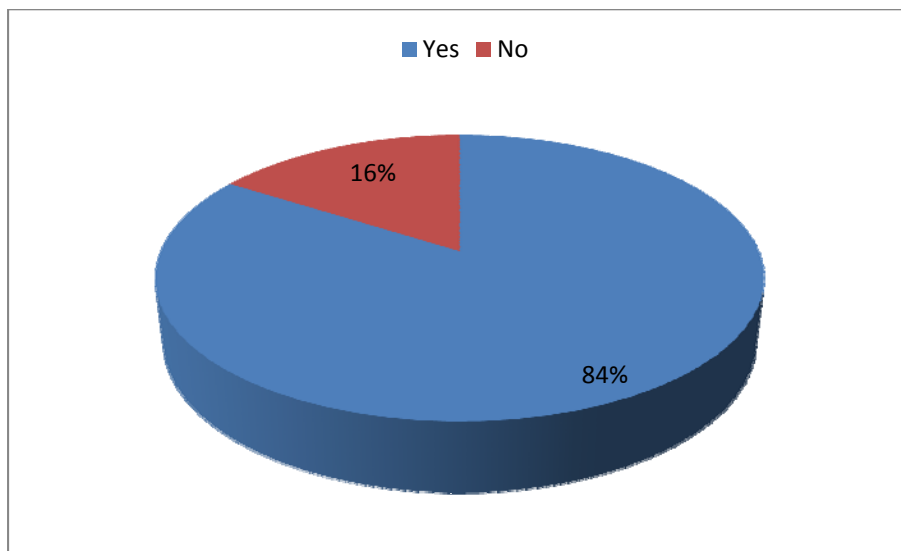
The respondents were able to give the following challenges of carrying out information system audit.

Costly in terms of installing and maintenance of the system, data can easily be manipulated by some workers that have access, data can be lost due to viruses and computer crashing, breakdown of the system, poor standards of equipments suit the information system design, network failure which makes the business to remain at a standstill and it require computer skills.

#### **4.8 Compliance audit and financial performance**

The research was also interest in finding out from the respondents whether compliance audit was carried out by the businesses within Katwe Butego division Masaka Municipality. The study was carried out on the contribution for doing this. The researcher wanted to know the contributions of compliance audit in the businesses within Katwe Butego Division. The results were as follows.

**Figure 4 a pie-chart showing whether compliance audit is practiced in the business**



**Source: Primary data, 2017**

In the figure above shows that the majority of the respondents 67(84%) agreed that compliance audit contributes to the financial performance of businesses in Katwe Butego Division Masaka Municipality and 13(16%) never agreed with it. It was revealed that compliance audit was practiced and it has the following contributions which were given by the respondents. It helps the business to its set goals and objectives thus improving its performance, enables the business to embark on carrying out proper book keeping and also prepare the required financial statements. This improved its adherence to GAAP thus stimulating its performance, detect fraud and errors, collecting information detect illegal acts ,helps to know whether the accounts have been prepared in accordance with the act of the firm's constitution ,promotes proper tax assessment, helps to follow the correct procedures when auditing, ensure that all standards required to boost performance are observed hence enhancing customer service and profitability of the businesses in the long run, it has led to the smooth running of the financial activities

without interference with in the business. This is in line with what was said by R .Walker (2009) that efficient use of board members 'time by stream line reporting to audit is a great benefit for the improvement of business governance by enabling the board members to move efficiently when fulfilling their duties for oversight of ethics and compliance as well as overall risk management and internal controls.

### **Challenges in carrying out compliance audit**

The respondents were able to give me the following challenges they face when carrying out compliance audit.

Inadequate knowledge about financial literature, suspicious crop out between different departments, expensive, scarcity of professional accountants, inadequate information to use, failure of financial managers to give adequate information to areas where necessary in case of losses. Some reports which are relevant are hidden from the auditor, inadequate time; technical skills are still lacking, corrupt management, incomplete records, expensive since it involves some expenditure in form of fees.

### **How has internal auditing increase financial performance of your business?**

It strengthens the business internal control system thus reducing on the fraud, mistakes and misstatements.

It helps the business to achieve its set goals and objectives since financial statements are well prepared and consistent thus stimulating financial performance.

Helps the management in decision making process hence increasing the financial performance of the business

It gives assurance and credibility to the accounts to the benefit of potential investors.

It has led to proper allocation of funds which has curbed losses.

It safeguards assets.

Ensures compliance with statutory regulations

Improving efficiency in operations.

Increasing financial integrity.

Ensures proper record keeping

I identify areas of improvement

Checks on the business performance and minimizes costs that would result from weak internal control system.

### **Challenges of internal audit**

**Table 11: Showing the challenges of internal audit**

<b>Challenges</b>	<b>Frequency</b>	<b>Percentage (%)</b>
Dishonest clerks with intension to commit errors and frauds.	5	6.25
Costly in terms of administration.	11	13.75
Inadequate knowledge	13	16.25
Inadequate funding	6	<b>7.5</b>
At times reports are not taken seriously by management	1	1.25
Managers often times refuse to pass on information to cover up their misuse of funds.	2	2.5
Prone to fraud	4	5
Lack of professional accountants	<b>5</b>	<b>6.25</b>
Poor record keeping	10	12.5
Poor allocation of financial resources	3	3.75
Poor perception of auditors	1	1.25
Bribery	9	11.25



Lack of monitoring process	1	1.25
Lack of management support	5	6.25
Corruption	3	3.75
Negligence of the Auditor	1	1.25
Total	80	100

**Source: primary data 2017**

From the findings above, it is revealed that majority of the respondents chose inadequate knowledge as the most challenge in carrying out internal audit 13(16.25%), followed by costly in terms of administration 11(13.75), Poor book keeping 10(12.5%), bribery 9(11.25%), inadequate funding 6 (7.5%) ,lack of professional accountants, monitoring process and dishonest clerks have the same respondents 5(6.25%), fraud 4(5%), poor allocation of financial resources and corruption have the same respondents 3 (3.75%), managers often times refuse to pass on information to cover up their misuse of funds 2(2.5%).Lastly negligence of the auditor, poor perception and at times are not taken serious by management have the same respondents of 1(1.25%) and this affected internal audit which hindered financial performance of the businesses

## Possible solutions

<b>Solutions</b>	<b>Frequency</b>	<b>Percentage</b>
Employing the external auditors to carry out auditing in the business.	2	2.5
Increase the funding of internal audit section.	5	6.25
Give adequate attention to the reports produced by internal audit section.	10	12.5
Businesses should aim at employing qualified people with skills and experience in auditing.	20	25
Regular meetings should be conducted to check on the business performance.	2	2.5
For any cases of fraud, businesses should find out the proper ways of punishing employees involved.	1	1.25
Hire honest people with ethical values.	3	3.75
Internal control should be employed to avoid fraud like regular inspections.	1	1.25
Reporting financial statements to form an opinion whether the balance sheets, profit and loss account are in agreement with the books of accounts and the returns .this can be done by use of bank reconciliation.	1	1.25
Measures, maximum supervision and monitoring should be conducted or done.	4	5
Hiring professional accountants.	6	7.5

Boosting good record keeping.	7	8.75
Inductions should be done on how to carryout internal auditing.	3	3.75
Introduction of a metric stream solution to help in management of a wide range of audit activities.	1	1.25
Following the audit standards.	11	13.75
Increased sensitization.	3	3.75
Total	80	100

**Source primary data 2017**

From the table above it is revealed that majority of the respondents gave a solution of employing qualified people with skills and experience in auditing 20(25%), followed by following the audit standards 11(13.75%), adequate attention to the reports produced 10(12.5%), boosting good record keeping 7(8.75%), hiring professional accountants 6(7.5%), increasing the funding of internal audit section 5(6.25%), measures maximum supervision and monitoring should be done 4 (5%),hire honest people with ethical values, inductions and sensitization have the same respondents of 3 (3.75%), employing external auditors and regular meeting have the same respondents 2(2.5%), proper ways of punishing employees involved in fraud, reporting financial statements, internal control should be employed and introduction of a metric stream solution to help in management of a wide range of audit activities have the same respondents of 1 (1.25%).

## **CHAPTER FIVE**

### **SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATION**

#### **5.0 Introduction**

This chapter presents summaries of the study findings as per the study objectives, conclusions based on those findings and recommendation which are based on both the study findings and other relevant literature considered necessary and vital to be used in future to improve the study situation.

#### **5.1 Summary of the findings**

In the findings of the study, it was revealed that the majority of the respondents were males with certificate holders and they were accountants, they had worked for between 20-30 years.

This findings show that majority of the respondents agreed that the financial audit was practiced with in the businesses of Katwe-Butego Division Masaka municipality and minority disagreed.

It was revealed that financial audit was commonly used by using bank reconciliation method and it was carried out monthly.

The findings revealed that majority of the respondents agreed that information system audit was practiced in the businesses of Katwe-Butego Division Masaka Municipality and the minority disagreed.

It was revealed that information system audit detects fraud and errors, helps to prepare the reports in time, ensures that information security is maintained and helps the user department to assess whether their business's financial statements are consistent with regard to GAAP hence contributing to the financial performance.

However some businesses did not carry out information system audit because they did not have an outstanding information system, ignorance, expensive and needs qualified personals.

Majority of the respondents in the findings from the study agreed that compliance audit was practiced in the businesses of Katwe-Butego Division Masaka Municipality and minority disagreed

The findings in the study showed that majority of the respondents answered this question which meant that they knew the contributions of internal auditing and they know how it has increased financial performance of the businesses.

However very few respondents from the study answered the challenges that affected internal auditing in their businesses such as dishonest clerks, expensive, inadequate knowledge and some solutions were given to them.

## **5.2 Conclusions**

From the study findings, internal auditing is seen as the most important tool for detecting fraud and errors in the business which helped to improve on the financial performance of the business.

Basing on the findings of the study, the results showed that some businesses faced challenges such as corruption, poor record keeping, dishonest, unqualified personal which affected financial performance of the businesses.

## **5.3 Recommendations**

Since it was evident in the study the staffing in internal audit department is not adequate, evidenced by not carrying out regular internal audit activities, not operating efficiently as well as their reports not being regular, the study therefore recommends competence profiling which should be based on what the small business expects the internal audit to do and what appropriate number of staff would be required to do this job.

The researcher recommends that small scale business establishes a strategy for improving the generation of additional finances. This could be done through writing projects, other competitive endeavors which are directly aimed at winning funds for the small scale business industry.

Furthermore, the researcher recommends that internal audit could be enhanced in-house training programs and control self-assessment questionnaires to create more awareness to staff of the roles and duties of internal auditors to enable audit services such as advisory services to run smoothly.

The researcher also recommends that small scale business should establish and manage knowledge information management system within the operations so as to enable all the parties within the business to freely access and utilize the official information.

Finally, the researcher recommends that there should be a deliberate attempt to conduct a study which establishes a relationship of management's commitment based on factors that are external to the small scale businesses in Katwe-Butego Division Masaka Municipality such as behavioral issues of the employees, financial crisis and information technology.

#### **5.4 Suggestions for further research**

- Determine the effects of internal audit work on the audit strategy.
- Assess the competence and objective of the internal auditor.
- The influence of ICT on the effectiveness on internal control system.

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## APPENDIX II

Dear Respondent,

I am Nakayima Rosemary, a student of Uganda Martyrs University pursuing a bachelor's degree in Business Administration and Management. I am conducting a study on **“The contribution of internal auditing on the financial performance of the small scale businesses in Katwe Butego Division Masaka Municipality”**. The information given by you is of great importance to my research and will be handled with maximum confidentiality.

### Questionnaires

#### Section A: Background information

In this section, tick the box that applies to you

1. Gender

Male  Female

2. Age

a. 20-30  b. 30-40

c. 40-50  d. 50-60

e. above 60

3. Level of work experience

a. 1-3years  b. 4-6years

c. 7-9years  d. Over 10 years

4. Your position in the business

- |                     |                          |                           |                          |
|---------------------|--------------------------|---------------------------|--------------------------|
| a. Internal Auditor | <input type="checkbox"/> | b. Accountant             | <input type="checkbox"/> |
| c. Finance manager  | <input type="checkbox"/> | d. Chief internal Auditor | <input type="checkbox"/> |
| e. Chief Accountant | <input type="checkbox"/> | f. Others                 | <input type="checkbox"/> |

If other specify .....

5. Professional qualification

- |                      |                          |                          |                          |
|----------------------|--------------------------|--------------------------|--------------------------|
| a. Bachelor's degree | <input type="checkbox"/> | b. Post graduate diploma | <input type="checkbox"/> |
| c. Diploma           | <input type="checkbox"/> | d. Master's degree       | <input type="checkbox"/> |
| e. Others            | <input type="checkbox"/> |                          |                          |

If other specify .....

6. Number of workers in the business

- |             |                          |            |                          |
|-------------|--------------------------|------------|--------------------------|
| a. Below 20 | <input type="checkbox"/> | b. Over 20 | <input type="checkbox"/> |
|-------------|--------------------------|------------|--------------------------|

**Section B: Financial audit and financial performance of small scale business**

1. Is financial audit being practiced in the business?

- |     |                          |    |                          |
|-----|--------------------------|----|--------------------------|
| Yes | <input type="checkbox"/> | No | <input type="checkbox"/> |
|-----|--------------------------|----|--------------------------|

2. If yes please list the contributions

.....  
.....  
.....  
.....

If no specify why

.....  
.....  
.....  
.....

3. How often does your business carry out financial audit
- a. Once a week       b. Monthly       c. Twice a week
- d. Quarterly       e. Annually

4. Tick the methods used by the business when carrying out financial audit

- a. Posting checking       b. Bank reconciliation
- c. Inspection       d. Confirmation
- e. Costing checking       f. Observation
- g. Inquiry       h. Physical examination

5. Challenges in carrying out financial audits

.....

.....

.....

.....

**Section C: Information systems audit and financial performance**

1. Do you carryout information systemsm audit in your business
- Yes  No

If yes what is the contribution of the information system audit

.....

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If no specify why

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.....

2. Challenges of carrying out information systems audit

.....

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**Section D: Compliance audit and financial performance**

1. Do you carryout compliance audit in your business

Yes

No

2. If yes state the contribution of compliance audit on the financial performance of the business

.....  
.....  
.....  
.....

If no specify

.....  
.....  
.....  
.....

3. Challenges of carrying out compliance audit in your business

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.....  
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**SECTION E**

1. How has internal auditing increased financial performance of your business

.....  
.....  
.....  
.....

2. In your view, what are the challenges of internal auditing to your business

.....  
.....  
.....  
.....

Give possible solutions

.....  
.....  
.....  
.....

**THANK YOU**